

# LOGISTICS & TRUCKING INDUSTRY REPORT

2020



## **BR Williams Trucking, Inc.**

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# Introduction and Market Recap

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The 2019 truckload freight market suffered a reciprocal backlash from the extreme capacity shortage of late 2017 and the first half of 2018.

The ELD-Mandate effectively removed 4% of truckload capacity from the market, while simultaneously increasing costs and decreasing revenues for truckload carriers. For truckload carriers, market conditions began deteriorating rapidly during Q3 of 2018. This occurred due to a confluence of factors but the most impactful factor being surplus capacity.

Orders for Class 8 heavy-duty trucks reached a backlog of a full year and thus when market equilibrium was realized in July of 2018, capacity was still contracted for future delivery, causing capacity to continue to be added to a market that desperately needed it to stop.



## Introduction and Market Recap

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Concurrently, the driver market began to loosen and demand for truckload capacity tempered. This sent spot market rates plummeting in an environment where costs had been rapidly rising for truckload carriers.

The spread between average spot rates and truckload carrier operating costs rose to its highest level since 2009.

Further, fresh off the caustic freight market of 2018, shippers moved away from the spot market and toward the safety of contract rates. Therefore, those carriers that were most vulnerable to the spot market struggled mightily and many did not survive.

According to the FMCSA and FTR Transportation Intelligence, 13,482 carriers and 34,906 tractors were removed from the truckload capacity market through September of 2019.

After September, bankruptcies began increasing rapidly and included the largest bankruptcy in truckload carrier history, Celadon.

At nearly 3,000 trucks, this added to an estimated 50,000 power units removed from the capacity pool during 2019 and the bleeding has not stopped. While this represents only 3.5% of the total tractor-trailer capacity market, this capacity was to play a critical role in absorbing several impending market shocks.

These shocks in aggregate may exceed the initial effect of the ELD mandate that caused the aforementioned capacity shortage. Without the surplus capacity to absorb the impact, capacity will yet again be in shortage.

This time around, however, there are several key differences that we will explore, along with the shocks themselves.



# 2020 Market Outlook

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The following is an examination of the truckload freight market for 2020 and the various factors that will exert pressure on it. After the extreme highs of late 2017, the first half 2018 freight market softened significantly, as manufacturing activity slowed and then stabilized.

This stable state has persisted throughout 2019. The problem was that the market was consistently poor for truckload carriers and as a result, many of them did not survive or reduced the size of their fleets.

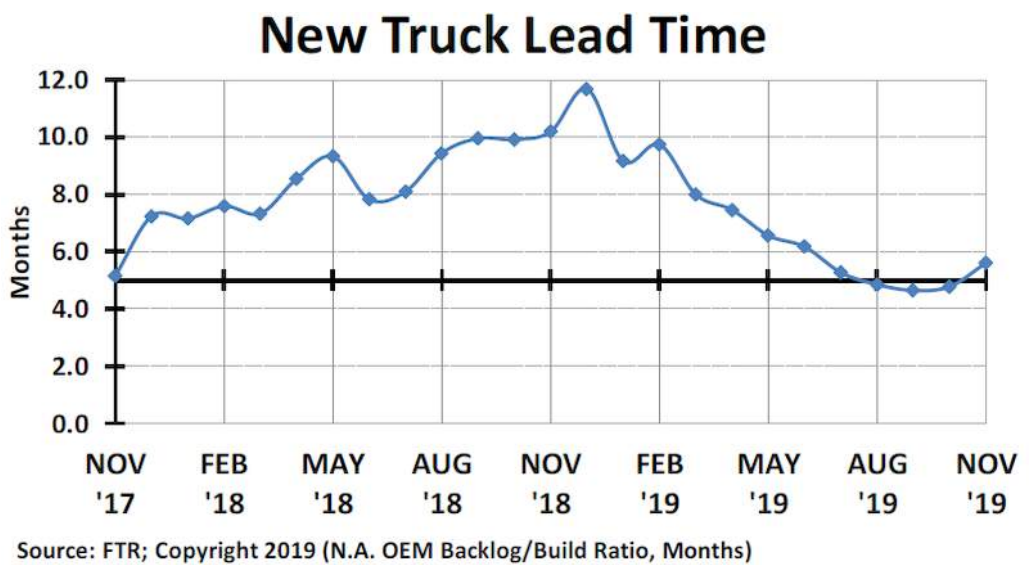
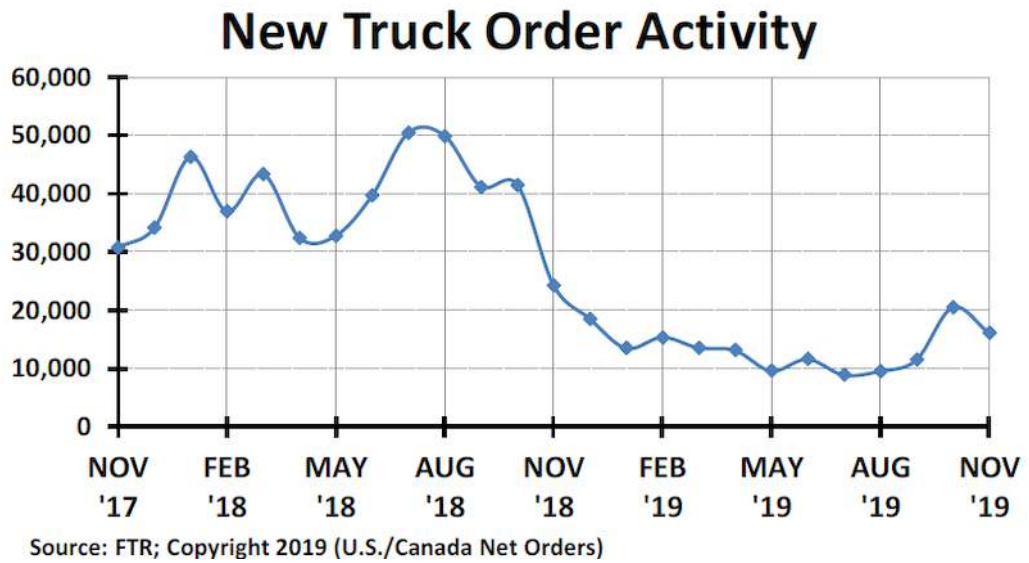
The surplus capacity necessary to absorb the shocks to the market without significant market disruption has been removed and now the outcome is likely yet another capacity shortage.

The impending shocks to the 2020 truckload freight market are as follows: The final ELD Mandate (eliminating all exceptions), the Drug and Alcohol Clearinghouse, IMO 2020, California's AB 5 rule, the USMCA trade agreement, and lastly, significant liability insurance rate increases. The first five are all regulatory or legislative in nature.

The last, however, liability insurance increases, is ironically borne of a lack of regulation. With all of these market shocks coming in close succession, they should remove 3-6% of tractor-trailer capacity. Unlike in 2018, equipment lead time is very short, allowing the market to respond to additional demand more quickly.

However, with 2019 still large in the rearview mirror, we do not expect a healthy appetite for new equipment in 2020.

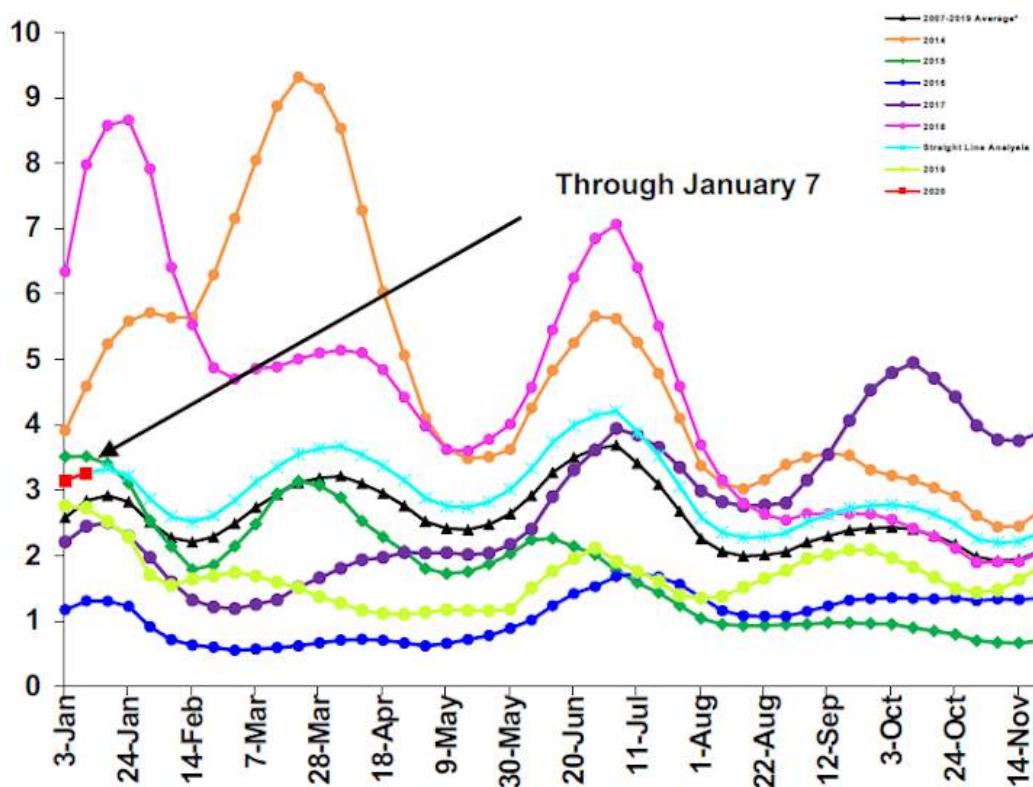
2020 Market Outlook



## 2020 Market Outlook

The Morgan Stanley Truckload Freight Index depicts the degree to which supply is meeting demand. A high data point illustrates tight capacity supply and upward pressure on rates, and a low data point, the opposite. The data suggests a rapid and super-seasonal tightening of capacity in Q4:

Exhibit 2: Morgan Stanley Dry Van ONLY Truckload Freight Index



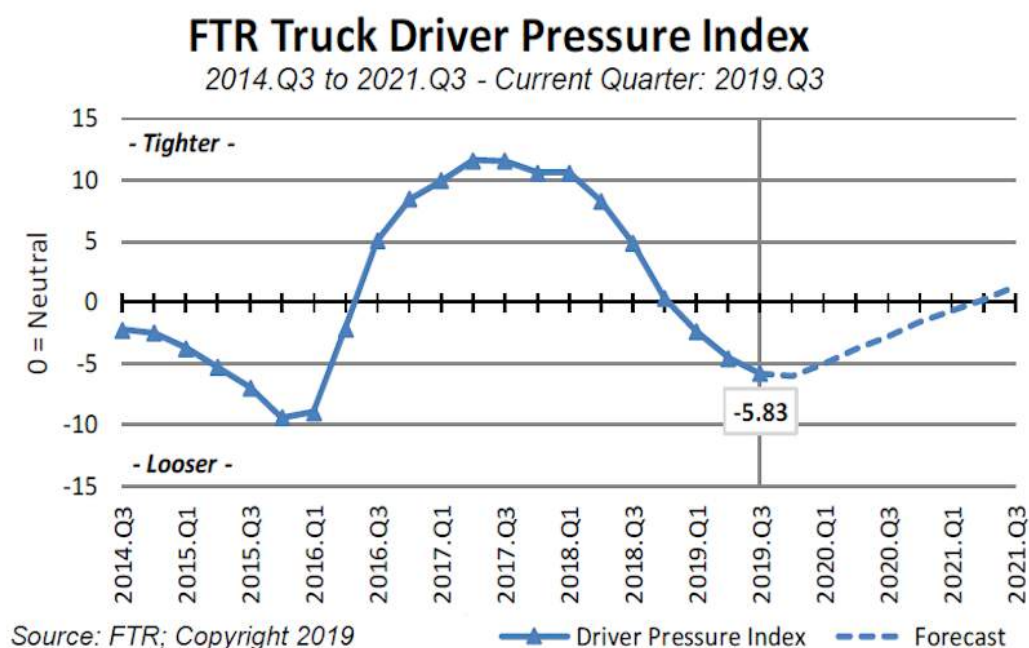
Another significant difference heading into this tight capacity phase vs the previous is that shipper profit margins, particularly retailers, are down. This means that they have fewer resources with which to absorb increases in transportation costs.

## 2020 Market Outlook

They are, however, more acutely aware of these issues and many augmented their transportation procurement strategies as a result, insulating themselves from the volatility of the spot market. There was a definitive shift among shippers from the spot market loads and 3PL's to contract rates and asset-based carriers.

The driver supply has loosened significantly since the peaks of shortage in early 2018. The driver market, however, is expected to tighten again during 2020. Some of the reasons for this are long-term and established.

The Baby-Boomer truck drivers are retiring out and being replaced with younger drivers that don't care to drive over the road. Some of the forecasted tightenings has new causes though. The Drug and Alcohol Clearinghouse will have significant effects here (more on this later).

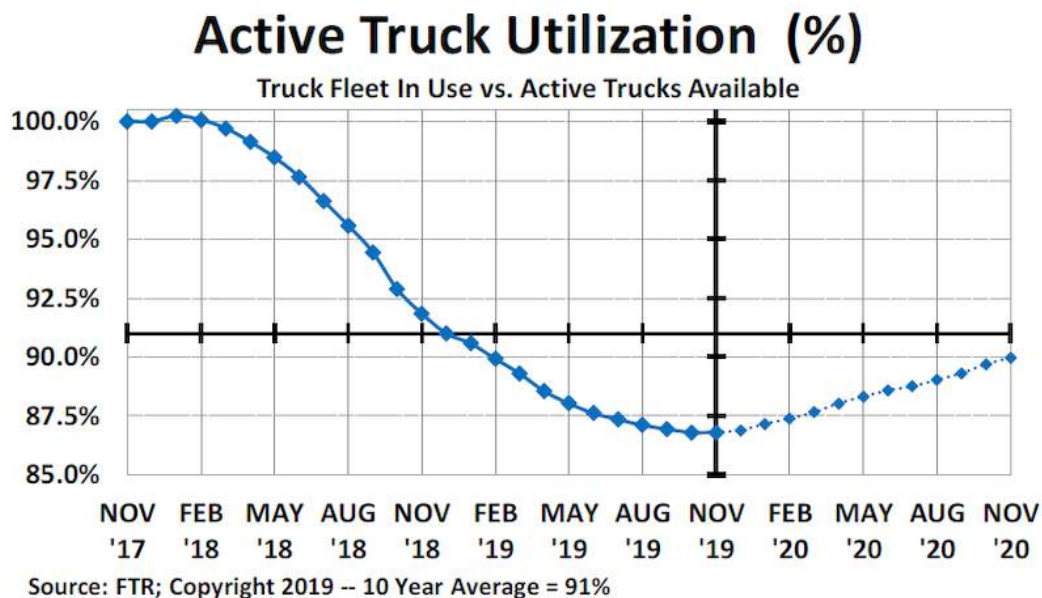




## 2020 Market Outlook

One measure of the health of truckload carriers is the “Active Truck Utilization” that measures the percentage of carriers’ fleets with seated drivers that are running on any given business day.

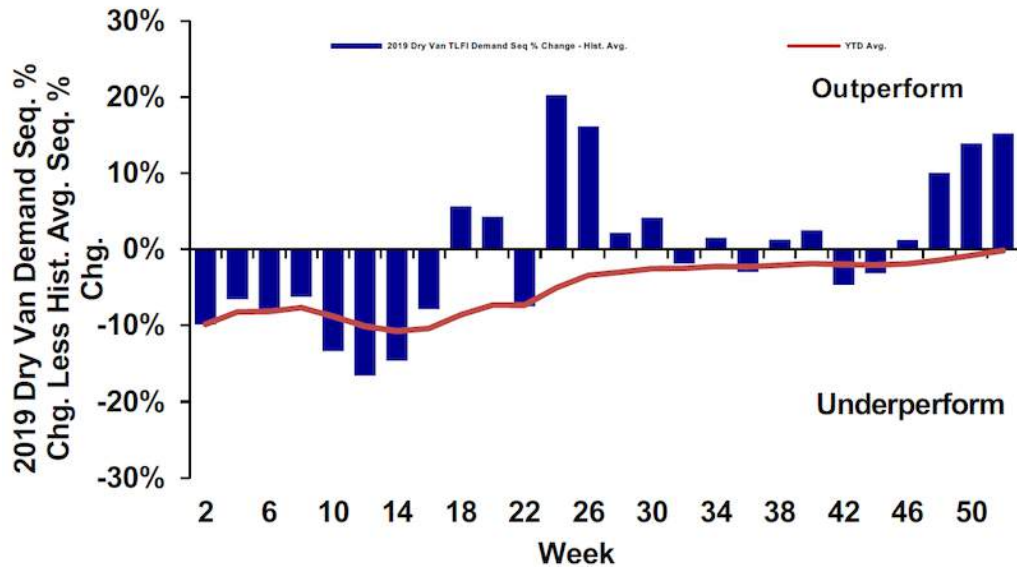
A 90% score would mean that the average carrier had 10% of their seated (with driver) fleet idle on business days. With the recent exodus of capacity, it is fair to assume that following is conservative and that the Utilization rate should improve more rapidly.



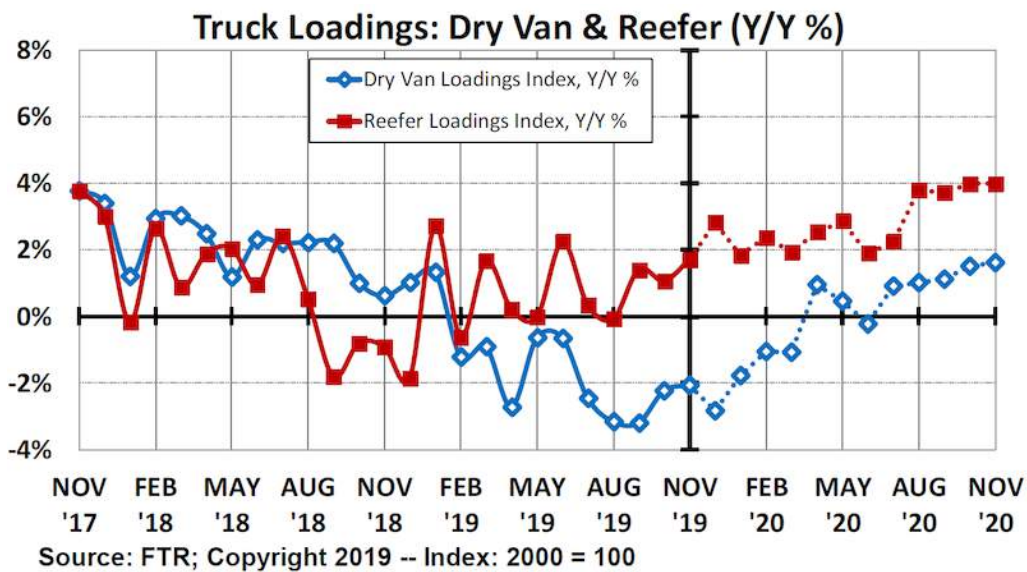
The supply component has been nearly solely responsible for the wild truckload freight market swings of the last twenty-eight months. Our forecasts assume a rather healthy or static demand component and that is supported in the data.

## 2020 Market Outlook

**Exhibit 4:** 2019 Dry Van DEMAND Seq. % Change Less Historical Average Seq. % Chg.

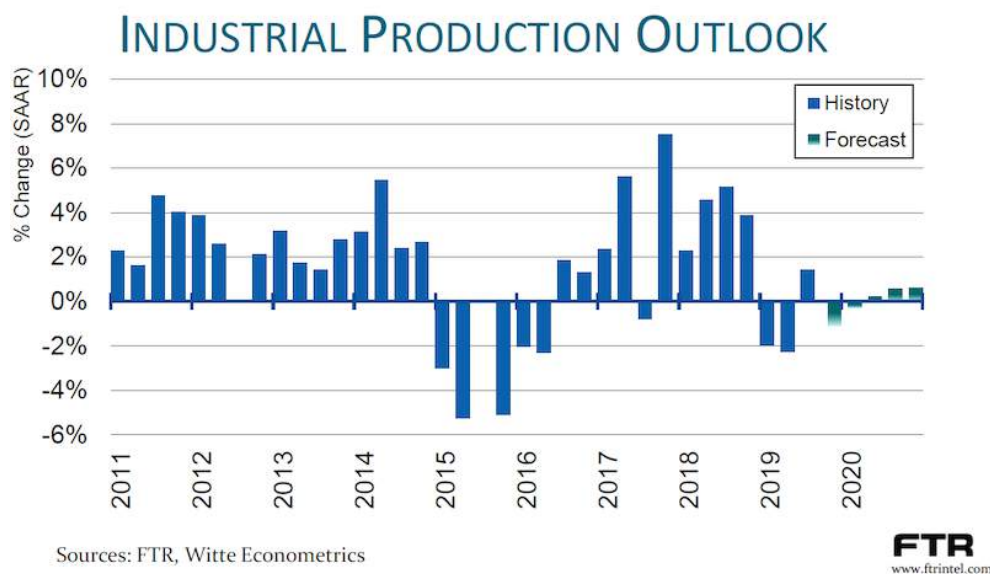


Source: Morgan Stanley Research



## 2020 Market Outlook

If the demand component, driven by the general economy, begins to experience unanticipated weakness, the market could be far more balanced than our forecast suggests. However, at this time, the general economic data appears to remain healthy and stable. Industrial Production Growth has tempered and stabilized. This is of concern because it is very truckload-intensive in nature.



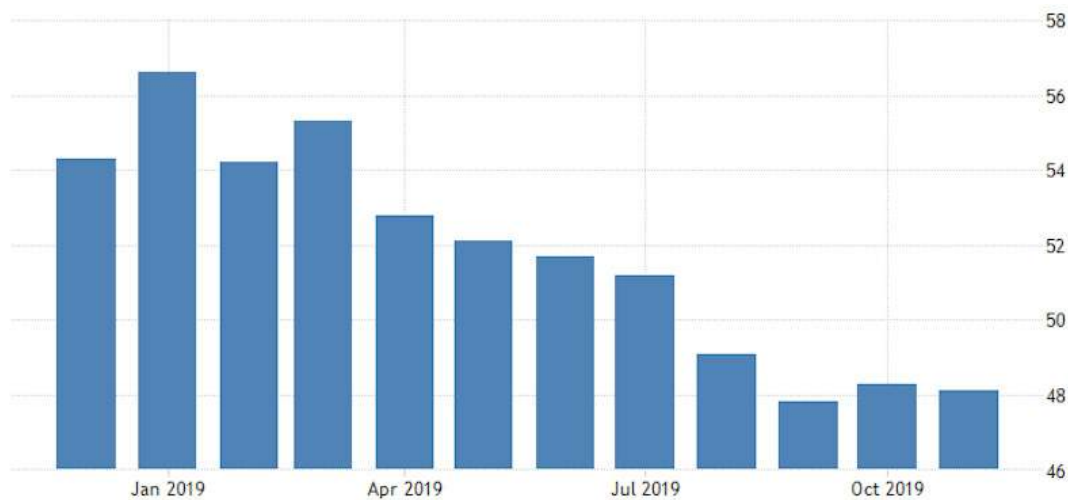
However, consumer spending, wages, unemployment, consumer confidence, and housing numbers remain strong.

The US Purchase Managers Index indicates the expected manufacturing activity levels of US factories. There has been a steadily declining trend since January 2019. The uncertainty in issues surrounding tariffs and global trade has had the most impact on these numbers. The trend appears to have bottomed out and stabilized.

## 2020 Market Outlook

As trade agreements appear to be solidified with assurances of meetings to sign proposed agreements, it is expected that factory activity should improve throughout 2020. Depending on the pace of improvement, and to what degree more tractor capacity is removed, much incremental growth in factory output, will affect the supply/demand ratio, as capacity cannot be added back easily under current conditions.

United States ISM Purchasing Managers Index (PMI)



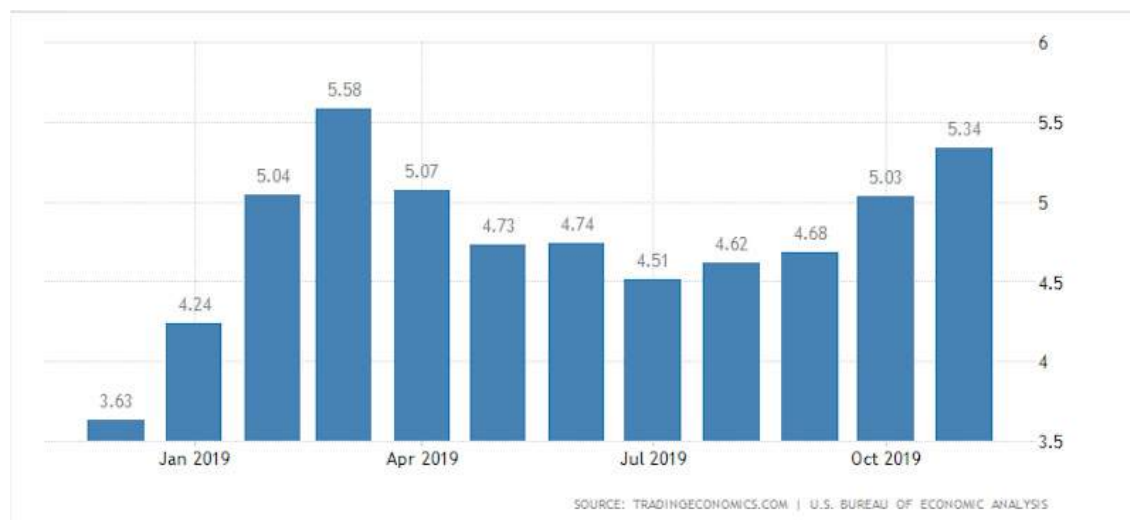
Consumer Spending Growth



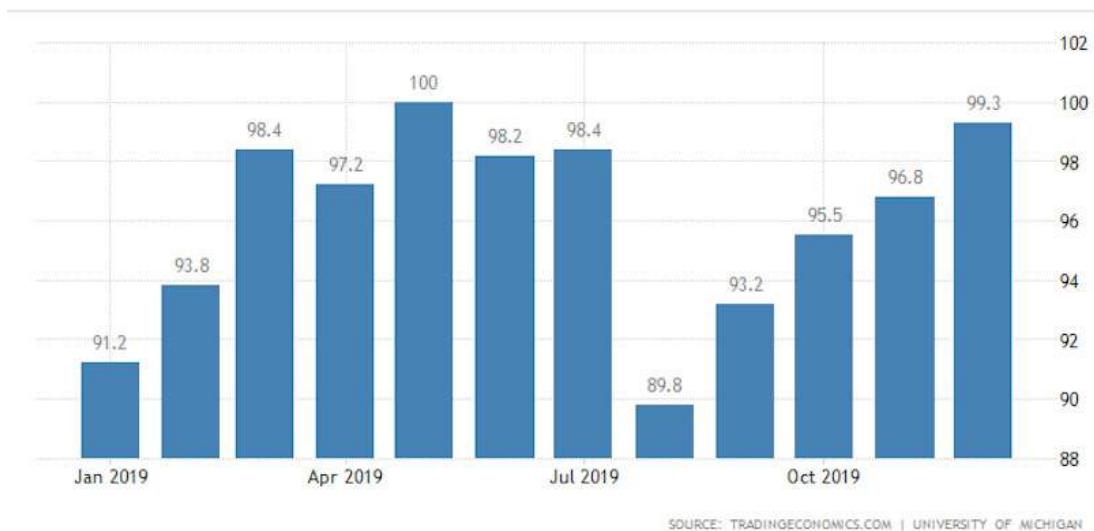


## 2020 Market Outlook

### U.S. Wage Growth year-over-year



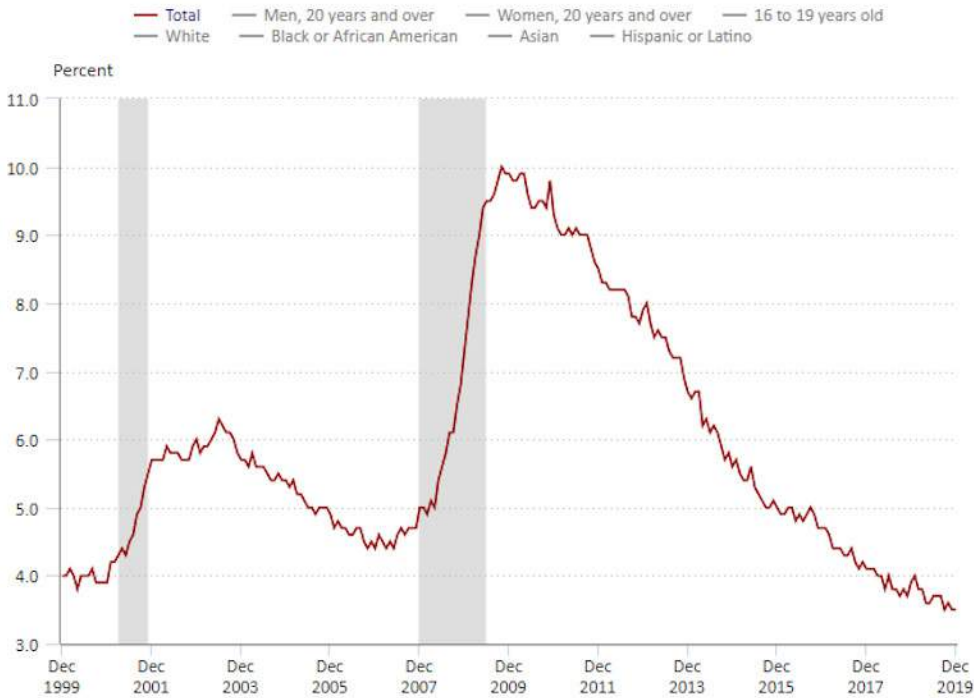
### US Consumer Confidence



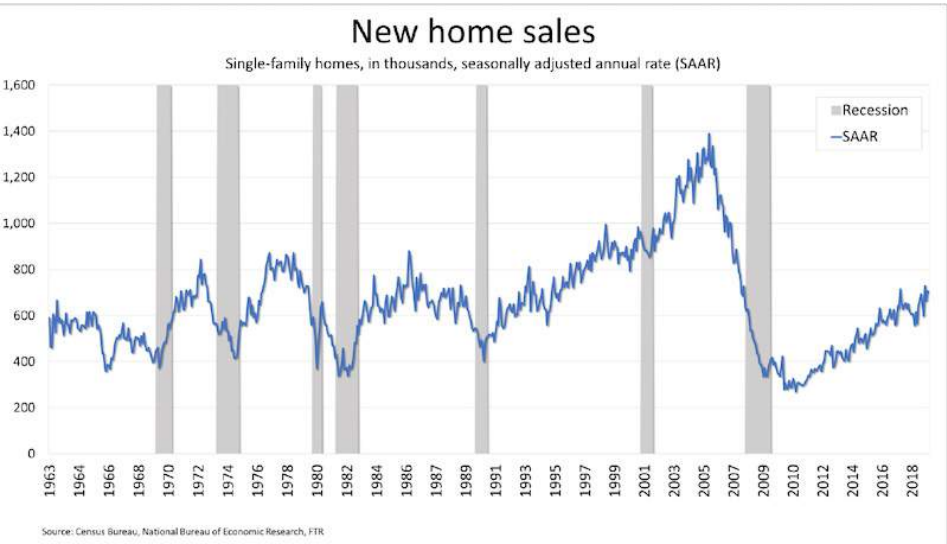
## 2020 Market Outlook

Civilian unemployment rate, seasonally adjusted

Click and drag within the chart to zoom in on time periods



Hover over chart to view data.  
 Note: Shaded area represents recession, as determined by the National Bureau of Economic Research.  
 Persons whose ethnicity is identified as Hispanic or Latino may be of any race.  
 Source: U.S. Bureau of Labor Statistics.



# Regulatory Environment

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## Liability and Umbrella Insurance

The trucking industry is experiencing the hardest market for liability insurances in recent memory.

This has been affected by the increasing number of recent “nuclear verdicts” being awarded across the country, combined with a history of insurance carriers tolerating multiple years of poor loss ratios due to being subsidized by other lines of insurances.

This year of reckoning has resulted in many carriers’ liability and umbrella coverages increasing by double-digit percentages. These are not small increases for trucking companies and will have to be passed along eventually.

Failure to renew or obtain competitive insurance rates is having a considerable impact on the trucking carrier failings and bankruptcies. Insurance renewals will be impacted throughout 2020, and are not expected to improve at least for the short term.

Insurance companies are getting increasingly selective in choosing companies that have a strong culture of safety and track record for claims.

Expect more news regarding this issue throughout 2020, as this factor is heating up and will impact supply issues through 2020 and pressures regarding rates.

## Final ELD Enforcement

The final enforcement date requiring full Electronically Logging Devices actually occurred on December 17.

As many carriers have already made the transition in anticipation of this enforcement date, the industry might see a slight impact during the first quarter of 2020, as more drivers will be placed out of service or marginal hit to productivity as a result of the full ELD technology.

## Regulatory Environment

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ELD's differ from the older technology in several ways but suffice it to say that full ELD's are much more precise in monitoring driver activity with fewer opportunities for manipulation or editing of actual on-duty activity, thereby placing all drivers to drive and comply with accurate real-time service hours regulations.

If we see any issues as a result of this final enforcement date, we expect it to be very small and short-lived (no more than 90 days), compared to other industry issues.

## IMO 2020

The trucking industry had to adapt to low sulfur diesel and more restrictive emissions regulations years ago.

However, the International Maritime Organization beginning January 1, 2020, now requires all ocean-going vessels to make the switch from high-sulfur fuel to similar low-sulfur options. As land and sea modes will now be consuming the same product, there could be shortages initially resulting in higher diesel fuel prices going into 2020.

We have seen a 10 cent increase in per-gallon costs since June 2019, a small portion being seasonal pricing. Depending on how these transitions for maritime, it could impact long term pricing upwards for diesel fuel.

This will affect everyone that has fuel surcharge agreements in place with trucking companies, and could actually affect the viability of smaller carriers that do not have such cost protection in place.

We should know very early on in 2020 what incremental impact this new regulation will have on the trucking industry. Our industry (and nation for that matter), has been blessed with some of the most stable energy costs for the last 2 to 3 years.

Hopefully, this trend will continue to contribute to more stable and dependable growth in our economy. As a side note, many states are increasing fuel taxes incrementally to pay for increased costs in the building and maintenance of roads and bridges.



## Regulatory Environment

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Alabama has already passed a 6 cent per gallon increase in diesel and gasoline effective September 2019, with another six cents to be added incrementally over the next 6 years. Surrounding states to Alabama have already increased by larger amounts. This will inevitably result in the base for diesel fuel national averages affecting fuel surcharges increasing nationally as well.

## California AB 5 Legislation

California has currently declared war on the use of owner-operators, or contract labor in our industry. The trucking industry depends heavily on the availability of owner-operators as a source of capacity.

California's real targets for this legislation are Uber and Lyft drivers along with Amazon delivery drivers. These business models depend almost solely on contract labor to fill their capacity needs. The unintended consequence though puts the trucking industry owner operators directly in the target sights of this legislation.

California has chosen a three-part test applied absolutely (known as the ABC test, and further, failure of any of the three prongs, results in failure overall), whereby companies are barred from utilizing contract labor for anything they are in the actual business of providing.

For example, a trucking company could utilize a plumber that is a contract laborer to repair plumbing issues. However, they would be barred from using contract labor to perform the same driving and delivery services their company employee drivers are performing.

The end result of the legislation is attempting to force companies to have only employees with full benefits.

This of course only currently impacts trucking companies based in California (or have very substantial operations there), although the long-term effect of this legislation depends on the State Courts followed by the Federal Courts handling of this issue.

## Regulatory Environment

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There continues to be a strong contingency of individuals that only prefer to operate as an owner-operator, providing them with much more autonomy than be employed by a company.

If this legislation is held to be valid and constitutional locally and finally nationally, this could result in another large pocket of available drivers be removed from the supply in our industry.

The California law was to go into effect January 1, however, a United States District Judge, Robert T. Benitez at the last minutes granted the California Trucking Association a temporary restraining order enjoining enforcement at least until after the motion for preliminary injunction hearing on January 13, 2020.

Also, Uber and Postmates have joined in a lawsuit in Federal Court, alleging that the AB-5 legislation violates several parts of both the United States and California Constitutions. Both these actions will at least temporarily delay enforcement of AB-5.

The monitoring of this ongoing issue is recommended. However, the immediate impact is remote for our customer base during the period that this has had a chance to work through all the attempts to block actual enforcement.

However, in the long-term, it would most assuredly impact our industry. BR Williams will continue to provide ongoing information to its customers regarding this issue.

## Drug and Alcohol Clearinghouse

Beginning January 6, 2020, all positive drug tests, refusals to submit to testing and evidence of actual drug use must be reported to a centralized database known as the Drug and Alcohol Clearinghouse.

Currently, carriers are required to request and provide drug test results as a part of mandatory background checks for commercial driver's licenses (CDL) drivers. With many states legalizing marijuana usage, however, federally it is still illegal and further disqualifies individuals from acquiring or maintaining a CDL.

## Regulatory Environment

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The Federal Motor Carrier Safety Administration found that although the industry was having a 1 % fail rate, drivers could easily find employment at other companies, and simply omit the company where the positive drug test occurred from their application records, thereby reducing detection of subsequent employers.

Mandatory reporting of all positive results to this clearinghouse would put an end to this practice going forward. Currently, FMCSA requires carriers to randomly test over 25 % of their average number of driving positions but also requires the FMCSA to increase the random testing rate, should national results indicate positive drug tests in excess of 1 % of all tests given.

Well, in fact, the results of the 2018 FMCSA Drug and Alcohol Testing Survey indicated that 2018 positive drug tests did exceed the 1 % benchmark. Therefore, FMCSA has just announced within the past week that they will require all carriers to now test at a pace of 50 % of average driving positions beginning January 1, 2020.

This will double the annual random drug tests performed, and it is estimated that at an average cost of \$28 to \$30 per test, this change will cost the industry between \$50 Million to \$70 Million annually.

Clearly, from a safety standpoint, we all want to remove unsafe drivers from our highways, and the immediate impact will be minimal.

One point to consider is that as of January 6, the clearinghouse will have no test results on file. It will only begin to record positive tests from that point forward. So, the impact will build and will be long term, as the process will work to weed out habitual users.

However, as national trends ease on the acceptability of some drug use, this issue could arise in importance going forward.

Lastly, on this issue, the majority of carriers utilize urine testing for drug tests. Studies have been completed and results indicate that hair follicle testing is a much more effective tool, even though urinalysis is the only FMCSA approved testing method at this time.

## Regulatory Environment

We expect at some point in the near future that hair follicle testing will be required, resulting in more failure rates (currently running at a positive test rate of 10 times the 2019 urine testing results) as drugs can be detected longer in hair.

Urine sample testing recognizes the last 3 to 4 days of drug behavior, whereas hair follicle testing recognizes drug behavior as far back as 90 days. This will result in identifying more of habitual users that have been able to avoid detection through the random testing and semi-annual re-certifications currently taking place.

Should FMCSA make the move to hair follicle testing in the future, this will accelerate a return to a tight driver market depending on the other variables that also impact the driver labor environment.

## USMCA Trade Agreement

The proposed United States-Mexico-Canada trade agreement is a much-improved agreement over its predecessor NAFTA. Some of the most obvious improvements economically include:

- De Minimis Thresholds – US shipments to Canada will no longer have import duties applied if the value of the product is \$150 or less (up from \$20, a 750 % increase). US shipments to Mexico will no longer have import duties applied if the value of the product is \$100 or less (up from \$50, a 100 % increase). Imports coming into the United States are expected to not have import duties applied if the value is \$800 or less. These increases in the De Minimis rules, should positively impact online purchases dramatically.
- Exemptions for Agricultural Products that were the policy under NAFTA, have been extended to be included in the USMCA agreement, whereas earlier drafts removed these exclusions.



## Regulatory Environment

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- Automobile Industry – USMCA agreement requires that vehicles manufactured within Mexico and Canada must have an average salary for labor building vehicles above \$16 per hour. This will also be indexed going forward and combined with new collective bargaining provisions being mandated, this should result in improved working conditions and quality of life for citizens of Mexico and Canada. Rules relating to the auto parts industry were also enhanced.

These and many other impactful positive provisions of the proposed USMCA Trade Agreement should provide a much improved economic win for each of the countries in the North American continent.

The final approval and signing of this document should result in the continuation of the rising tide going forward, and further should continue to pile on to the momentum of improving the general US economy in the second half of 2020 as predicted throughout this document.



# Conclusion

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Assuming a static general economy and demand component with the possibility of improvement in the second half of 2020, the rash of bankruptcies in the second half of 2019 has set up another perfect storm of factors all pointing toward a rapid and severe tightening of capacity.



The coming “shocks” to the truckload freight market have been known for some time.

However, until the recent rash of bankruptcies, the expectation has been that sufficient surplus capacity existed to absorb those shocks and that perhaps, they would merely eliminate the surplus and balance the market at a point that is reasonably healthy for all participants.

This is no longer the case. One mitigating factor is that many shippers moved away from spot pricing and to the relative safety of contract pricing with dedicated capacity, or chose to expand their first-party or private fleet strategies.

A factor that may prove beneficial to some shippers and detrimental to others is the timing of these market forecast revisions. For those shippers that locked in pricing with dedicated, asset-based carriers in 2020, they will most certainly out-perform the market.

## Conclusion

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For those shippers that locked in pricing with brokers or small, non-dedicated asset-based carriers and budgeted based on that, will likely find themselves revising budgets mid-year. Routing guide compliance will slip and tender rejections should explode.

The last tight capacity cycle began in earnest in September 2017. This timing allowed for revisions and preparations to be made for 2018.

While few were prepared for the severity of the 2018 truckload freight market, fewer still were oblivious at the time that strategies, contracts, budgets, and forecasts were set for 2018. For 2020, the timing of these changes and forecast revisions were not as kind.

There is little in the general economic data that would support a slowdown in 2020. Thus, the demand component should remain strong.

In fact, all three of the economists we follow are now indicating that manufacturing and overall economic activity will pick up from current levels starting around mid-year 2020, and will continue to build through the end of the year, with sustainability after that point depending on the results of elections in November 2020.

They all three are also now in agreement that the chance of a recession in 2020 is very small. All of these factors indeed add up to capacity crunch that is somewhere within the range of the previous tight capacity cycle in late 2017 and early 2018.

## Recommendations

The following are some recommendations that BR Williams has for its shipper partners:

- Flee the spot market for contract pricing
- Open dialogues with your carrier base to take their temperature regarding 2020 expectations

## Conclusion

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- Reiterate with brokers and non-dedicated asset-based carriers the importance of tender acceptance/routing guide compliance in maintaining a long-term partnership
- Find ways to provide more advance notice of load tenders as this will increase routing guide compliance
- Avoid expedites and unexpected capacity issues with more effective planning and safety stock
- As how your 3PL sources capacity and the characteristics of their typical carrier? If your 3PL specializes in cheap trucks, there is a very good chance that they operate almost entirely on the spot market, which renders their shipper customers far more vulnerable to the spot market than a 3PL that specializes in high-quality capacity (established, safe carriers). Ask them how.
- As we fully expect for the shipping community to be competing for capacity in 2020, find ways to make your freight more attractive for the least amount of investment and trouble:
- Limit detention with better planning
  - Consolidate specialized freight (hazmat, tanker endorsed, freeze protect) into as few loads as possible
  - Keep weights under 44,500 lbs
  - Allow for the use of refrigerated units for dry freight
  - Utilize drop trailers and live load
  - Allow for flexible ship/deliver days where possible





## ABOUT BR WILLIAMS TRUCKING, INC.

*With humble beginnings back in 1958, [BR Williams](#) has grown into an award-winning supply chain management company servicing all 48 contiguous states and Canada. With facilities in [Mobile AL](#); [Piedmont, AL](#); [Tallahassee, FL](#); [Anniston, AL \(two facilities\)](#); [Eastaboga, AL](#); and [Oxford, AL](#), B.R. Williams' distribution network supports over 50 customers and another 2,550 in the [Trucking](#) and [Logistics](#) divisions. Industries served include the following: automotive, defense, home improvement, education, food raw materials, textiles, chemical, industrial packaging, metals (finished goods), highway safety and more.*

*To discuss your Distribution, Logistics, or Transportation Services options, please contact [sales@brwilliams.com](mailto:sales@brwilliams.com) or [\(800\)-523-7963](tel:(800)523-7963).*

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